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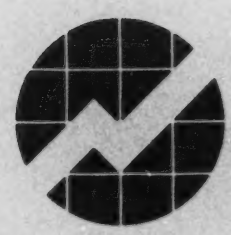
KEDI ECONOMIC SURVEY

OCTOBER ISSUE

October 31, 1979



KENT ECONOMIC AND DEVELOPMENT INSTITUTE

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KEDI ECONOMIC SURVEY

OCTOBER ISSUE

October 31, 1979

President: Vladimir J. Simunek

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In this issue, the 1979:3 Index of Industrial Production has been selected for comparison. Almost all forecasters underestimated the actual development.

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1.0 OVERVIEW AND ASSUMPTIONS

1.01 OVERWIEW

KEDI's projection of only a mild decline remains essentially unchanged from the September issue, as third quarter data substantiated our prediction of an increase in the real GNP and the raise of the Federal Reserve discount rate to new record heights.

The economic outlook was briefly brighter as the GNP rose at a seasonally adjusted 2.4% during the third quarter, making up for the second quarter slump of 2.3%. As predicted, the Federal Reserve Board has raised the discount rate to 12%.

As these data support our previous forecast, the scenario remains unchanged: there will be no full-scale recession. The economy is expected to decline during the fourth quarter, and bottoming out during the first quarter of 1980. Sluggish growth is expected throughout 1980 and 1981, with the start of recovery in 1982.

The quarterly forecast data of real growth and income have been raised somewhat, due to routine adjustments from preliminary third quarter data regarding production and factory orders. Monetary and credit data have been reduced a little.

KEDI forecast for 1980, as compared here with data released by other leading economic forecasters, are more optimistic about the growth and unemployment rate, but gloomier about the inflation rate. All are convinced that recovery will begin by the middle of next year, however.

KEDI: The real GNP for 1980 will level off, with a recovery beginning in

in the second quarter of 1980. Unemployment will go to 7.3% in the first quarter 1980 and then will gradually decline. Inflation rate will go down to 8.3% when measured by the GNP implicit price deflator, and 10.1% when measured by the Consumer Price Index. A combined tax-expenditure measure will be adopted in the second quarter of 1980.

Data Resources, Inc.: Real GNP will decline about 2.0%, with recovery beginning during the first quarter of 1980. Unemployment will go to 7.3% and inflation will get down to 9.0%. No tax cut is seen until 1981.

Chase Econometric Associates, Inc.: Real GNP will decline about 2.5%, with recovery beginning in the second quarter of 1980. Unemployment will go to 8.0% and inflation will get down to 8.0%. A $ 25 billion tax cut is predicted effective April 1, 1980.

Wharton Econometric Associates, Inc.: Real GNP will decline about 1.6% with recovery beginning in the first quarter of 1980. Unemployment will go to 7.5% and inflation will decrease to 8.5%. A $ 20 billion tax cut is predicted effective January 1, 1980.

Merill Lynch Economics,Inc.: Real GNP will decline about 2.5% with recovery beginning in the first quarter of 1980. Unemployment will go to 7.7% and inflation will drop to 7.9%. A $ 20 billion tax cut is predicted effective January 1, 1980.

Adding to the uncertainty about the economic outlook are vague and somewhat contradictory statements by Administration officials. Paul Volcker, Federal Reserve Board chairman, has maintained that the Fed's current tight-credit policies could soon lead to an economic turn-around and lower interest rates. Volcker has also said that the Fed will resist any political pressures to ease these policies.

Treasury Secretary G.William Miller has assured Congress that the Carter Administration is prepared to bolster the economy with alternative measures should the recession prove deeper than expected under the Fed's new policies, although president Carter has spoken of supporting the policies even though it may hurt him politically.

President Carter has also held out hope that interest rates and inflation have "peaked" and will now be decreasing instead of spiralling upward. However, the Business Council, a private group of top corporate executives, has concluded that the Fed's measures may mildly deepen an economic downturn.

Most economists agree, in general, that if the recession will develop deeper than expected, the Administration will have to come with some fiscal and monetary measures to help the economy. But the views on the extent of such measures and their timing differ widely. KEDI expects some bolstering of the economy by the Administration to occur in the first half of the year 1980, but this help will not turn the trend dramatically upwards. Forecast of this Institute shows the sluggish pace and slow growth of the economy throughout the next two years, with indications of the start of the new cycle appearing markedly not earlier than in the first half of the year 1981.

The KEDI forecast of the developments in the U.S.economy is highlighted on the following page in Table 1.0.

1.02 ASSUMPTIONS

The following assumptions are parts of this forecast. Compared with

KEDI FORECAST HIGHLIGHTS

Table 1.0

Indicator	Unit	1978	1979	1980	1985
Gross National Product	bil. 1972$	1399.2	1425.1	1423.9	1712.1
Index of Industrial Production	1967 =100	145.2	151.6	151.6	167.1
Capacity Utilization	%	84.3	84.8	80.8	86.4
Unemployment Rate	%	6.0	6.0	7.0	6.1
Private Housing Starts	mil. units	2.020	1.751	1.603	1.898
Car Sales	mil. units	11.3	10.6	10.0	12.4
Implicit GNP Price Deflator	1972 =100	152.1	165.5	179.3	272.9
Consumer Price Index	1967 =100	195.3	217.4	239.3	371.0
Producer Price Index	1967 =100	209.3	237.0	270.1	399.2
Federal Deficit	bil.$	-27.7	-9.4	-16.4	-20.3
Personal Income	bil.$	1717.4	1917.2	2163.2	3244.1
Prime Rate	%	9.06	12.86	13.42	9.90
Mortgage Rate	%	9.30	10.32	11.24	9.72
Currency plus Demand Deposits	bil.$	352.8	376.4	414.6	640.1
Commercial and Industrial Loans	bil.$	230.9	265.1	279.5	440.2

assumptions incorporated into the September, 1979, forecasts, the changes concern the Assumption No.9. In the forecast, the factory orders, defense orders, orders for machine tools, and export orders have been increased. That is the second consecutive increase in these categories since August 1979. Also the indicators of consumers' and businesses confidence have been raised somewhat.

1. In 1979 and 1980, approximately 95% of the demand for oil in this country will be met. In 1981 all basic U.S. demands for oil should be met. The weighted price of oil in 1979 will average $24 per barrel and in 1980 this figure will go up to the $28 range. In 1981, it is expected the price will go up on $33 and in 1982, on $38 per barrel.

2. The supply of Iranian oil will settle to a normal flow in the second part of 1980.

3. Starting third quarter 1979, the Administration will pursue the policy of maintaining high interest rates and tight money. In the second or third quarter of 1980 it will adopt fiscal measures aimed against further increases in unemployment. The monetary policy will ease during this same time.

4. It is assumed that in 1981 the new Administration will adopt a definite program in fighting the inflation by gradually reducing the excess demand. The Federal Reserve Board will, at long last, begin a policy of setting the limits to the monetary growth by <u>long-term</u> commitments, not just short-term as has been the policy in the past. Price and wage controls must remain the last resort of stabilization policy.

5. Our foreign trade with China will expand more rapidly starting the end of this year, and will gain a substantial momentum in 1980 and 1981.

6. This year, the U.S. will experience a good harvest and the U.S.S.R. an extra low one. In 1980, 1981, and 1982 good harvests are assumed for this country and average production of crops is expected in the U.S.S.R. Low harvest in the U.S.S.R. is expected in 1983.

7. It is projected here that the rates of growth in 1979, 1980, and 1981 in the major industrial countries will be as follows for real GNP:

	1979	1980	1981
West Germany	3.0%	3.1%	3.4%
Italy	2.9	3.0	3.1
Japan	3.2	3.5	3.7
Great Britain	1.4	1.8	2.1
France	2.8	2.9	3.0

8. No abrupt changes in political situations in the world will occur.

9. The attitude of businesses and consumers will remain at low levels in 1979 and throughout 1980. A significant change is assumed to occur in 1981, due mainly to the Administration's policy aimed to stimulate the increases in productivity in the economy.

1.1 REAL GROWTH

(Table 01. on page 7)

KEDI does not expect any dramatic downturn in the economy during the coming months. The predictions for quarterly values of the GNP and the Index of Industrial Production have been changed slightly upwards, due mainly to third quarter 1979 data recently announced by the U.S.Department of

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TABLE 01. REAL GROWTH
(Unless otherwise noted, quarterly data are seasonally adjusted at annual rates)

Indicator	Unit	1978*	1979				1979
			1*	2*	3	4	
Gross National Product, 1972$	bil.$	1399.2	1430.6	1422.3	1430.8	1416.7	1425.1
Index of Indust. Production	1967=100	145.2	151.5	151.8	152.1	151.1	151.6
Unemployment Rate	%	6.0	5.8	5.7	5.8	6.6	6.0
Capacity Utilization Rate	%	84.3	86.0	85.8	84.9	82.6	84.8
Private Housing Starts	mil. units	2.020	1.616	1.837	1.826	1.724	1.751
Car Sales	mil. units	11.3	11.7	10.9	10.0	9.7	10.6

Indicator	Unit	1979	1980				1980
			1	2	3	4	
Gross National Product, 1972$	bil.$	1425.1	1410.3	1415.2	1428.4	1441.5	1423.9
Index of Indust. Production	1967=100	151.6	149.8	151.4	152.3	152.9	151.6
Unemployment Rate	%	6.0	7.3	7.0	6.7	6.8	7.0
Capacity Utilization Rate	%	84.8	80.3	79.9	80.3	82.5	80.8
Private Housing Starts	mil. units	1.751	1.490	1.604	1.671	1.647	1.603
Car sales	mil. units	10.6	9.3	9.6	10.3	10.6	10.0

Indicator	Unit	1980	1981				1981
			1	2	3	4	
Gross National Product, 1972$	bil.$	1423.9	1445.6	1459.7	1469.8	1487.5	1465.7
Index of Indust. Production	1967=100	151.6	153.1	153.9	155.2	155.9	154.5
Unemployment Rate	%	7.0	6.1	6.4	6.2	6.3	6.3
Capacity Utilization Rate	%	80.8	83.4	83.9	84.3	85.4	84.3
Private Housing Starts	mil. units	1.603	1.549	1.708	1.801	1.842	1.725
Car sales	mil. units	10.0	10.4	11.2	11.3	11.7	11.2

Commerce and the Federal Reserve Board.

The forecast shows that the expected decline in the economy during the coming two quarters will be lead by a drop in (1) automobile sales; (2) declining sales in automobile-related industries such as steel, rubber and machinery; (3) a decline in the housing industry, and (4) a decline in paper and forest products industries.

However, indications are that the slumps in the automobile and housing industries will be less severe that during the previous recession in 1974-1975.

% changes from previous quarter

Housing Units Starts				Car Sales			
Last Recession		Forecast		Last Recession		Forecast	
1973:3	-5.8%	1979:3	-.6%	1973:3	-4.1%	1979:3	-8.3%
4	-18.6%	4	-5.6%	4	-16.3%	4	-3.0%
1974:1	-3.4%	1980:1	-13.6%	1974:1	-6.1%	1980:1	-4.1%
2	-4.4%	2	+7.7%	2	0.0%	2	+3.2%
3	-20.6%	3	+4.2%	3	+12.0%	3	+7.3%
4	-14.9%	4	-1.4%	4	-31.1%	4	+2.9%
1975:1	-4.7%	1981:1	-6.0%	1975:1	+18.3%	1981:1	-1.9%
2	+9.7%	2	+10.3%	2	-6.0%	2	+7.6%

Comparison of the above data indicates that projected declines will be less severe than those which occured in 1973-1975.

Actual situations and some forecasts confirm the view of this Institute. On the other hand, some forecasters paint a gloomy picture of coming months. For example, homebuilders foresee a collapse of their industry. The National Association of Home Builders maintains that housing starts will plummet 44% during 1980, resulting in the loss of 675,000 jobs in the building trade and 818,000 jobs in related fields.

Other industries, that will be affected by the expected slump, are less

pessimistic. For example, steel makers have reduced their projections of shipments of steel in the year 1980 by a relatively small margin. Most steel executives assume, now, that the economic slump will last into 1980, but will be relatively mild. Some decline is also expected in recent forecasts for the paper, paperboard and forest products industries. The forecast expects 3-4% decline of output in the year 1980. Also the outlook for the rubber industry is cloudy. The forecast of this Institute shows a 1% decline in output of tires and rubber products in the year 1980.

While the above industries seem most affected by the expected economic downturn, the picture of other industries and areas of the economy does not seem as bad.

KEDI expects that consumer demand for nondurable goods will continue to be strong. Preliminary data show that October sales will be slightly above September's and indications are that sales will continue to grow in the coming months. Another positive sign is that consumer confidence turned upward in September, according to the Conference Board, a business research organization. The increase was the first of the year and was largely attributed to less anxiety about the gasoline supply and a downturn in unemployment. Positive developments have also appeared in the area of capital outlays: Machine-tool orders were 30% higher in September than a year earlier, apparently unaffected by higher interest rates and the economic slowdown. Factory orders were up 3.9% in September, evidence of the economy's uplift in the third quarter. Industrial production, led by the motor vehicle industry, increased in September, a temporary, but significant development.

1.2 PRICES AND NOMINAL GNP

(Table 02. on page 11)

KEDI's forecast of price developments has not been significantly changed. This Institute maintains its projection that the Consumer Price Index will grow by about 10% during the next year, with the Producer Price Index growing by 11% and the GNP price deflator by 8.3%. For this year, the KEDI forecasts are the respective 11.3%, 13.3%,and 8.9%.
The KEDI prediction for this year is supported by recently released data for September and recent forecasts of the Administration'economists.
The Administration's official forecast is a 10.6% price increase as measured by the Consumer Price Index for this year, although the Administration's chief inflation fighter, Alfred Kahn, does not think, the figure is "achievable".

In the area of consumer prices, KEDI maintains its forecast, that prices of meat, dairy products and other food will remain flat for the rest of the year, but will resume an upwards trend during the first half of 1980.

In the year 1980, besides the constantly growing prices of housing and energy items, the main increases are expected in household appliances and transportation services. Prices of furniture, carpets, apparel and upkeep will grow only moderately.

The picture remains gloomy in the area of producers' prices. No significant changes are shown for any item compared with the September forecast. Producers' prices will climb a monthly adjusted average 1% for the rest of this year and throughout the year 1980.

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TABLE 02. PRICES AND NOMINAL GNP
(Unless otherwise noted, quarterly data
are seasonally adjusted at annual rates)

Indicator	Unit	1978*	1979				1979
			1*	2*	3	4	
Consumer Price Index, NSA	1967=100	195.3	207.0	214.1	221.3	227.4	217.4
Producer Price Index, NSA	1967=100	209.3	223.7	231.5	242.1	250.6	237.0
Implicit GNP Price Deflator	1972=100	152.1	160.2	163.7	167.1	171.0	165.5
Gross National Product	bil.$	2107.6	2292.1	2329.8	2391.5	2422.6	2359.0
Personal Cons. Expenditures	bil.$	1340.1	1454.2	1475.9	1528.6	1558.7	1504.4
Gross Private Dom. Investment	bil.$	345.6	373.8	395.4	392.1	407.8	392.3

Indicator	Unit	1979	1980				1980
			1	2	3	4	
Consumer Price Index, NSA	1967=100	217.4	231.1	237.1	242.0	246.9	239.3
Producer Price Index, NSA	1967=100	237.0	258.5	263.3	273.9	284.5	270.1
Implicit GNP Price Deflator	1972=100	165.5	173.8	177.6	181.5	184.3	179.3
Gross National Product	bil.$	2359.0	2451.1	2523.4	2592.5	2656.6	2555.6
Personal Cons. Expenditures	bil.$	1504.4	1586.4	1610.2	1650.7	1690.8	1634.5
Gross Private Dom. Investment	bil.$	392.3	404.3	412.8	426.5	438.7	420.6

Indicator	Unit	1980	1981				1981
			1	2	3	4	
Consumer Price Index, NSA	1967=100	239.3	252.5	257.1	264.0	268.8	260.6
Producer Price Index, NSA	1967=100	270.1	286.2	293.4	300.6	306.7	296.7
Implicit GNP Price Deflator	1972=100	179.3	187.3	190.5	195.2	199.5	193.1
Gross National Product	bil.$	2555.6	2707.9	2781.2	2869.2	2967.6	2831.5
Personal Cons. Expenditures	bil.$	1634.5	1711.8	1751.3	1796.2	1830.2	1772.4
Gross Private Dom. Investment	bil.$	429.3	453.4	469.2	483.7	495.3	475.4

1.3 EMPLOYMENT AND LABOR

(Table 03. on page 13)

KEDI's forecasted unemployment rate for the fourth quarter has been slightly increased from 6.29% to 6.57% and by an average 0.3% during 1980. The increases are mainly due to the expected increases of numbers of unemployed persons in industries affected by the coming economic downturn. These industries are: automobile, housing, construction, rubber, paper, wood, furniture, household appliances, stone, clay and glass.

The projection shows that the long-heralded increase in unemployment will occur during the fourth quarter of this year and will continue in the first quarter of 1980. For the rest of the year, the prediction presents the following data for the unemployment rate: October 6%, November 6.5%, and December 6.8%. We expect the highest unemployment rate in the first quarter 1980, followed by gradual improvement throughout the remainder of the year and in 1981. The long-term projection shows significant decreases in unemployment rates not earlier than in the years 1982 and 1983.

1.4 HOUSING

(Table 04. on page 15)

KEDI's forecast in the area of housing is more optimistic than the forecasts of other agencies.

During 1980 we expect 1.056 million single-family units starts and .548 million multi-family starts. This is above the widely predicted 1.3 to 1.5 million units starts and the even more pessimistic projection of 1.1 to 1.3 million starts presented by the National Association of Home Builders.

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TABLE 03. EMPLOYMENT AND LABOR
(Quarterly data are seasonally adjusted at annual rates)

Indicator	Unit	1978*	1979				1979
			1*	2*	3	4	
Population	mil.	218.5	219.6	220.1	220.7	221.3	220.4
Civilian Labor Force	mil.	100.4	102.4	102.9	103.2	103.8	103.1
Employed	mil.	94.4	96.5	97.0	97.2	97.0	96.9
-Agriculture	mil.	3.3	3.3	3.3	3.4	3.3	3.3
-Non Agriculture	mil.	91.0	93.2	93.7	93.8	93.7	93.6
Unemployment Rate	%	6.0	5.77	5.73	5.81	6.57	5.97

Indicator	Unit	1979	1980				1980
			1	2	3	4	
Population	mil.	220.4	221.9	222.6	223.4	224.1	223.0
Civilian Labor Force	mil.	103.1	104.2	104.8	105.6	106.4	105.3
Employed	mil.	96.9	96.6	97.5	98.5	99.1	97.9
-Agriculture	mil.	3.3	3.3	3.4	3.4	3.3	3.4
-Non Agriculture	mil.	93.6	93.3	94.1	95.1	95.8	94.5
Unemployment Rate	%	5.97	7.26	6.98	6.71	6.81	6.94

Indicator	Unit	1980	1981				1981
			1	2	3	4	
Population	mil.	223.0	224.7	225.5	226.3	227.1	225.9
Civilian Labor Force	mil.	105.3	107.1	108.0	108.7	109.4	108.3
Employed	mil.	97.9	100.5	101.1	101.9	102.5	101.5
-Agriculture	mil.	3.4	3.3	3.3	3.4	3.3	3.3
-Non Agriculture	mil.	94.5	97.2	97.8	98.5	99.2	98.2
Unemployment Rate	%	6.94	6.14	6.43	6.22	6.27	6.27

More optimistic outlook have presented the economists of the U.S. League of Savings Banks. According to their forecast, the impact of increased mortgage rates and the Federal Reserve tight money policy will be not felt immediately, but with a lag of three to five months because of the lending commitments already made. It is expected that the housing sales will continue in the rest of the year and in the first quarter of 1980, and, if no relief will be provided during that time, a drastic decline in building activity would occur in the spring.

In the KEDI's current forecast, new housing prices have been considered. The average price of a single-family home has been increased by approximately 2% in 1981, and by 4% in 1982 and subsequent years. We now anticipate a stronger demand for new homes base on revised population projections. The new data show a persistent demand for approximately 2 million housing units for each year during the coming decade, which will lead to a new round of housing price increases just after the housing slump passes in 1980.

5.0 FEDERAL AND STATE AND LOCAL BUDGETS

(Table 05. on page 17)

The forecast data here have been changes slightly due to preliminary third quarter 1979 estimates recently released by the U.S.Department of Commerce. The projected Federal deficits have been increased because of higher projections of Federal expenditures connected with the expected economic downturn. Also the State and local governments' surpluses have been reduced somewhat in this projection due to the expected additional expenditures on unemployment benefits.

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TABLE 04. HOUSING
(Quarterly data are seasonally adjusted at annual rates)

Indicator	Unit	1978*	1979				1979
			1*	2*	3	4	
Single-Family Housing Starts	mil. units	1.433	1.119	1.262	1.238	1.164	1.196
Multifamily Housing Starts	mil. units	.567	.496	.575	.588	.560	.555
Mobile Homes Shipments	thous units	276	284	276	278	247	271
Housing Permits Issued	mil. units	1.680	1.405	1.503	1.302	1.256	1.367
Construction Costs-Commerc.	1972= 100	164.3	172.7	177.6	185.6	195.9	183.0
Construction Costs-Resident.	1972= 100	161.8	171.8	175.5	182.1	192.4	180.5
Indicator	Unit	1979	1980				1980
			1	2	3	4	
Single-Family Housing Starts	mil. units	1.196	.982	1.063	1.110	1.067	1.056
Multifamily Housing Starts	mil. units	.555	.508	.541	.561	.580	.548
Mobile Homes Shipments	thous units	271	219	230	241	251	235
Housing Permits Issued	mil. units	1.367	1.011	1.029	1.065	1.004	1.028
Construction Costs-Commerc.	1972= 100	183.0	198.9	203.7	212.8	217.8	208.3
Construction Costs-Resident.	1972= 100	180.5	194.0	201.5	208.9	214.6	204.8
Indicator	Unit	1980	1981				1981
			1	2	3	4	
Single-Family Housing Starts	mil. units	1.056	.999	1.127	1.192	1.193	1.128
Multifamily Housing Starts	mil. units	.548	.550	.581	.609	.649	.597
Mobile Homes Shipments	thous units	235	246	270	287	291	274
Housing Permits Issued	mil. units	1.028	.988	1.065	1.206	1.285	1.136
Construction Costs-Commerc.	1972= 100	208.3	221.8	226.0	230.4	240.8	229.8
Construction Costs-Resident.	1972= 100	204.8	217.0	221.3	224.5	228.5	222.8

The projection of the Federal deficit for the year 1981 is $22 billion, in contrast with the Administration's promise of a balanced budget in the fiscal year beginning October 1, 1980.

Again, our forecast does not incorporate a tax break, as the possibility of major tax cuts in 1980 seems even less likely. A compromise budget resolution recently reached by House and Senate conferees does not include any tax cut provisions, while setting a ceiling of $547.6 billion on outlays and a floor of $517.8 billion on revenue during the fiscal year. The Committee agreed to aim for a Federal deficit of $29.8 billion during the fiscal year 1979-1980, a higher figure than last year's $27.7 billion.

KEDI expects some fiscal measures will be adopted in mid-1980 to hold down unemployment and to boost consumer spending and business capital outlays (see Assumption No.3). This assumption has been built into all KEDI forecasts since 1976.

1.6 INCOME

(Table 06. on page 19)

A sharp decline in Personal Saving during the third quarter 1979 has caused major adjustments in KEDI's forecast data in the income category. Personal Saving dropped to $66.9 billion from an average $82.5 billion during the first two quarters of this year. Our projected data for Personal Saving for the fourth quarter of this year and the first two quarters of 1980 have been reduced, with a return to a more normal level in the second half of 1980.

KEDI has hit the target with its forecast of corporate after-tax profits for the third quarter 1979, preliminary data show. For the fourth quarter,

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TABLE 05. FEDERAL AND STATE AND LOCAL BUDGETS
(Quarterly data are seasonally adjusted at annual rates)

Indicator	Unit	1978*	1979				1979
			1*	2*	3	4	
Federal Govt.:							
Income Taxes	bil.$	189.4	207.4	220.6	229.4	235.8	223.3
Corporate Profit Tax Accruals	bil.$	72.0	77.2	74.9	79.7	80.1	80.0
Surpl./Deficit	bil.$	-27.7	-11.7	-7.0	-7.7	-11.2	-9.4
State and Local Governments:							
Income Taxes	bil.$	37.5	40.8	42.9	43.6	44.0	42.8
Corporate Profit Tax Accruals	bil.$	12.5	14.1	13.7	14.1	14.3	14.1
Surpl./Deficit	bil.$	27.4	27.6	19.7	21.2	19.1	21.9

Indicator	Unit	1979	1980				1980
			1	2	3	4	
Federal Govt.:							
Income Taxes	bil.$	223.3	238.2	242.3	248.7	251.4	245.2
Corporate Profit Tax Accruals	bil.$	80.0	80.1	82.0	86.0	91.2	84.8
Surpl./Deficit	bil.$	-9.4	-15.1	-16.7	-18.2	-15.4	-16.4
State and Local Governments:							
Income Taxes	bil.$	42.8	44.6	46.4	47.8	49.8	47.2
Corporate Profit Tax Accruals	bil.$	14.1	14.9	15.8	17.0	17.8	16.7
Surpl./Deficit	bil.$	21.9	18.9	17.3	15.7	16.6	17.1

Indicator	Unit	1980	1981				1981
			1	2	3	4	
Federal Govt.:							
Income Taxes	bil.$	245.2	256.6	258.1	267.4	270.1	263.1
Corporate Profit Tax Accruals	bil.$	84.8	93.0	96.7	102.3	107.8	100.0
Surpl./Deficit	bil.$	-16.4	-20.5	-21.6	-22.1	-26.4	-22.7
State and Local Governments:							
Income Taxes	bil.$	47.2	51.2	53.2	55.4	56.7	54.1
Corporate Profit Tax Accruals	bil.$	16.7	18.6	19.7	21.4	22.7	20.6
Surpl./Deficit	bil.$	17.1	18.7	21.2	24.0	25.6	22.4

we expect a further decline in profits of auto makers, and a decline in in the profits or increased losses of the airline, steel and rubber industries. In general, the corporate profit outlook for 1980 is optimistic. The projection shows steady increases in profits, despite the anticipated recession. This corresponds with the views of many Wall Street economic forecasters, whose projections rather a slowing of growth than a declining of profits. For example, the monthly summary prepared by the Institutional Brokers Estimate System, and based on projections of approximately 2.000 companies, shows the average 5.6% increase in profits in 1980 as compared with the year 1979.

Personal Income also is not expected to have any dramatic decline during the period of anticipated recession, although farmers' income is projected lower in 1980 than in 1979. Agriculture Department officials expect net farm income to drop to about $27 billion from the predicted $30 billion this year, a decrease of about 10%. The anticipated decrease is based largely on continuing high costs of fuel and fertilizer, officials say.

1.7 MONEY AND CREDIT

(Table 07. on page 21)

KEDI expects slower growth in the money supply throughout the fourth quarter of 1979 and the first quarter of 1980. Our forecast data of the money supplies M1 and M2 have been reduced due to (1) the revised October 3 and October 10 data recently released by the Federal Reserve Board, and (2) changes in Assumption No.9.

The projected data for monetary and credit aggregates show no drastic downturn during the rest of this year or in 1980. However, calculations,

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TABLE 06. INCOME
(Quarterly data are seasonally adjusted at annual rates)

Indicator	Unit	1978*	1979				1979
			1*	2*	3	4	
Personal Income	bil.$	1717.4	1852.5	1892.5	1943.5	1980.1	1917.2
Personal Dispos. Income	bil.$	1458.4	1572.2	1601.7	1636.9	1656.7	1616.9
Compensation of Employees	bil.$	1304.5	1411.2	1440.6	1471.8	1481.3	1451.2
Corp. Profits After Tax	bil.$	121.5	142.0	139.3	144.5	139.9	141.4
Personal Saving	bil.$	72.0	79.2	85.9	66.9	77.4	77.4
Average Weekly Earnings	$	203.3	212.4	217.8	222.6	226.3	219.8

Indicator	Unit	1979	1980				1980
			1	2	3	4	
Personal Income	bil.$	1917.2	2030.1	2140.7	2201.6	2280.3	2163.2
Personal Dispos. Income	bil.$	1616.9	1704.1	1756.1	1850.8	1970.3	1820.3
Compensation of Employees	bil.$	1451.2	1508.6	1602.1	1697.3	1762.1	1642.5
Corp. Profits After Tax	bil.$	141.4	140.0	146.9	160.1	167.4	153.6
Personal Saving	bil.$	77.4	82.3	87.3	90.4	92.3	88.1
Average Weekly Earnings	$	219.8	227.3	230.6	236.5	239.4	233.5

Indicator	Unit	1980	1981				1981
			1	2	3	4	
Personal Income	bil.$	2163.2	2340.2	2410.5	2480.7	2540.7	2443.0
Personal Dispos. Income	bil.$	1820.3	2004.3	2040.3	2121.5	2186.3	2088.1
Compensation of Employees	bil.$	1642.5	1800.6	1849.2	1953.1	1990.4	1898.3
Corp. Profits After Tax	bil.$	153.6	171.2	178.5	183.3	185.7	179.7
Personal Saving	bil.$	88.1	93.6	97.1	97.8	99.5	97.0
Average Weekly Earnings	$	233.5	242.7	248.7	251.6	262.8	251.5

conducted by this Institute show, that a credit crisis might occur if interest rates are pushed higher than present levels. A serious downturn might occur if the Federal Reserve discount rate reaches approximately 15%, with a corresponding 17% to 18% prime rate, and with the corresponding tight money Federal Reserve policy. The present 12% discount rate and 15 1/4% prime rate do not indicate a danger of a credit crunch.

Henry C.Wallich, member of the Board of Governors of the Federal Reserve System, also maintains that current interest rates seem "very unlikely" to cause a credit crisis. Pressures are mounting, however, for a further increase in the discount rate. Besides the domestic strong demand for credit, there is increasing pressure from outside. West Germany's central bank has raised its discount rate from 5% to 6%, the Netherlands bank from 8% to 8 1/2%, Canada to 14%, and it is expected that soon will the rates the central banks in France and Japan. These pressures on the dollar may well push the U.S. rate as much as full percentage point, according to some economists.

This leads to conclude that further hikes in interest rates are not unlikely. However, KEDI maintains its position that the period of tight monetary and credit policy is expected to last no longer than the first quarter of 1980.

1.8 INTEREST RATES, YIELDS AND SECURITIES PRICES

(Table 08. on page 23)

Further increases in interest rates are possible in the near future, as discussed in the previous section. Also, our forecast for long-term interest rates indicates that the market has not yet been stabilized. KEDI's projection shows that mortgage rates will reach an average 12.2% for residential

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TABLE 07. MONEY AND CREDIT
(Data for "Currency + Demand Deposits" and "Time Deposits, Adjusted" are averages of daily figures; other data are end of period figures)

Indicator	Unit	1978*	1979				1979
			1*	2*	3	4	
Currency+Demand Deposits	bil.$	352.8	357.0	373.8	382.4	392.2	376.4
Time Deposits, Adjusted	bil.$	580.2	618.7	635.2	643.1	659.7	639.2
Consumer Instal. Credit	bil.$	275.6	278.3	284.8	290.2	297.4	297.4
Commerc.and Ind. Loans at Banks	bil.$	230.9	243.5	255.2	259.3	265.1	265.1
Negotiable Cert.of Deposits	bil.$	96.6	99.0	103.9	111.9	114.8	114.8
Mortgages at S&L Assns.	bil.$	432.9	441.4	447.5	450.3	453.1	453.1
Indicator	Unit	1979	1980				1980
			1	2	3	4	
Currency+Demand Deposits	bil.$	376.4	402.4	411.7	419.8	424.5	414.6
Time Deposits, Adjusted	bil.$	639.2	667.8	680.3	696.7	718.6	690.9
Consumer Instal. Credit	bil.$	297.4	301.1	305.2	310.7	316.4	316.4
Commerc.and Ind. Loans at Banks	bil.$	265.1	267.1	269.3	272.8	279.5	279.5
Negotiable Cert.of Deposits	bil.$	114.8	120.6	127.2	130.3	132.3	132.3
Mortgages at S&L Assns.	bil.$	453.1	455.4	460.7	464.5	479.3	479.3
Indicator	Unit	1980	1981				1981
			1	2	3	4	
Currency+Demand Deposts	bil.$	416.4	430.3	436.8	449.8	460.3	444.3
Time Deposits, Adjusted	bil.$	690.9	728.2	746.8	759.3	778.9	753.3
Consumer Instal. Credit	bil.$	316.4	322.5	330.7	339.6	350.4	350.4
Commerc.and Ind. Loans at Banks	bil.$	279.5	283.4	295.9	310.6	319.5	319.5
Negotiable Cert.of Deposits	bil.$	132.3	135.4	140.7	147.9	158.6	158.6
Mortgages at S&L Assn.	bil.$	479.3	482.7	495.4	503.1	514.8	514.8

new mortgages by the end of the year and will not begin a decline until the second quarter of 1980.

The forecast data for interest rates on consumer loans have been almost unaffected when compared our current forecast with the forecasts presented in the first half of this year.

The stock market forecast does not indicate any significantly larger impact of the expected economic downturn on the price of stock. The projection of the Standard & Poors 500 average for the rest of the year shows small fluctuations around the 102 level, with significant increases during the second half of 1980.

2.0 COMPARISONS OF ACCURACY OF PREDICTIONS

In this issue, the Index of Industrial Production for the third quarter 1979 has been selected for comparison. Almost all forecasters underestimated the actual development. Actual data are taken from the FEDERAL RESERVE. Industrial Production. G.12.3, October, 1979 issue, Table 1-A, page 2. Forecast data are from Business Forecasts 1979, published by the Federal Reserve Bank of Richmond, Va., February 1979, Library of Congress Catalogue Card No: 75-189493. Table on page 24 shows the predictions of forecasters and the deviations of forecast data.

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TABLE 08. INTEREST RATES, YIELDS AND SECURITIES PRICES

Indicator	Unit	1978*	1979				1979
			1*	2*	3	4	
3 mo Treas.Bills Rate(new issues)	%	7.22	9.26	9.61	9.89	11.74	10.13
Prime Rate	%	9.06	11.75	11.75	12.31	15.63	12.86
Mortgage Rate, New Homes	%	9.30	9.97	10.05	10.17	11.12	10.32
Aaa Bonds Rate	%	8.73	9.29	9.54	9.72	9.97	9.63
Long Term Govt. Bonds Yield	%	8.48	9.03	9.19	9.36	10.47	9.51
Standard & Poor's 500 Average	1941-43=100	96.11	99.35	100.18	101.54	106.27	101.84

Indicator	Unit	1979	1980				1980
			1	2	3	4	
3 mo Treas.Bills Rate(new issues)	%	10.13	12.46	12.03	10.85	10.47	11.45
Prime Rate	%	12.86	15.68	14.01	12.56	11.42	13.42
Mortgage Rate, New Homes	%	10.32	11.57	11.41	11.02	10.94	11.24
Aaa Bonds Rate	%	9.63	10.24	10.15	10.06	9.73	10.05
Long Term Govt. Bonds Yield	%	9.51	10.76	10.64	10.12	9.78	10.33
Standard & Poor's 500 Average	1941-43=100	101.84	101.03	99.56	102.76	103.12	101.62

Indicator	Unit	1980	1981				1981
			1	2	3	4	
3 mo Treas.Bills Rate(new issues)	%	11.45	10.13	9.87	9.65	9.48	9.78
Prime Rate	%	13.42	11.06	10.14	9.73	9.28	10.05
Mortgage Rate, New Homes	%	11.24	10.57	10.36	10.06	9.87	10.23
Aaa Bonds Rate	%	10.05	9.47	9.27	9.20	9.36	9.33
Long Term Govt. Bonds Yield	%	10.33	9.65	9.54	9.47	9.42	9.52
Standard & Poor's 500 Average	1941-43=100	101.62	103.16	105.17	107.13	109.24	106.18

TABLE 2.0 COMPARISONS OF ACCURACY OF PREDICTIONS
INDEX OF INDUSTRIAL PRODUCTION

(third quarter 1979, 1967 = 100)

Actual: 152.1

Forecaster	Page in Business Forecasts 1979	Forecast	% of Accuracy
American Statistical Association and National Bureau of Economic Research	19	148.0	-1.4
Cyrus T. Lawrence, Inc.	21	145.2	-3.9
The First National Bank of Chicago	22	151.6	-0.1
General Electric Company	23	146.0	-4.1
University of California	25	145.1	-4.6
The Fidelity Bank	26	154.0	+0.1
Bankers Trust Company	27	150.4	-0.1
Chemical Bank	28	153.1	+0.1
KEDI	29	150.4	-0.1
Manufacturing Hanover Trust	30	145.9	-4.1
Argus Research Corporation	31	145.7	-4.1
Morgan Guaranty	32	149.7	-1.6